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March 10, 1995

The Honorable Reed E. Hundt
Chairman
Federal Communications Commission
1919 M Street, NW
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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

EX PARTE - CC Docket 94-1

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Dear Mr. Chairman:

On March 3, 1995 NYNEX filed an ex parte in CC Docket 94-1, entitled "A NYNEX Proposal for the LEC Price Cap Plan." GTE agrees with NYNEX that the FCC's price cap regulation of interstate access should promote effective competition, and that the degree of regulation in each market should be linked to the development of competition in that market. However, NYNEX's proposal would appear to mix the apples of state regulatory agencies' local competition policies with the oranges of FCC regulation and competition in interstate access markets.

The design of price cap regulation should be based on answers to these three questions:

- What is the relevant market?;
- What criteria should be used to evaluate competition?;
- How should price cap regulation evolve as competition develops?

GTE already has proposed a price caps plan on the record which provides clear answers to these questions. GTE urges the Commission to issue a Further Notice in this proceeding to gather the necessary record to adopt such a plan. In the interim the Commission should act to eliminate sharing for reasons presented below.

Our concerns with NYNEX's proposal, as well as GTE's suggestions for necessary price cap reform, are as follows:

(1) What is the relevant market?
NYNEX seeks to condition interstate price cap reform on the exposure of access lines to certain state policies toward local competition. GTE believes price caps reform should be conditioned on the state of competition in the more relevant market — interstate access. The FCC has jurisdiction over interstate access services. Its regulation of these services, and its efforts to enable and enhance competition for these services, should be firmly rooted in the relevant market, interstate access not local.

The local and interstate access markets are quite different. Competition is developing in many areas for interstate access, regardless of whether local dial tone competition has developed in those areas. As GTE has shown on the record, an enormous portion of the demand for interstate access is generated by large business customers. In Santa Monica,

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California, for example, more than 75% of GTE's interstate access demand comes from large end user locations that already are within reach of an alternative provider.

The alternative provider does not have to provide local service in order to compete for this access demand; nor do these customers have to change their local service provider in order to obtain access to an IXC from an alternative vendor. The access competitor need only connect the end user to an IXC location, not to all other local subscribers. NYNEX suggests that an access competitor may be discouraged from providing interstate access in a particular market area by the inability to provide intrastate access services in the same area. While some states have limited local dial tone competition, states generally have not prevented CAPs from providing connections to IXCs for intrastate access.

(2) What criteria should be used to evaluate competition?
The criterion to evaluate competition should be whether customers in the relevant access market actually have a choice of access service providers. In contrast, NYNEX proposes to condition steps in the price cap plan on the percentage of access lines to which a certain state's policies toward local competition apply. However, interstate access demand is highly skewed across access lines. In Santa Monica, the 75% of access demand that has competitive alternatives today is generated by less than 1.5% of all end user locations. Clearly, the lion's share of the access market could be subject to competition long before any criterion expressed in terms of access lines would be met.

By relying on state regulation and local market competitive indices, NYNEX's criteria could trigger the relaxation of price cap regulation in interstate access markets where no competition exists, while preventing LECs from responding where it does. Further, the existence of certain state policies toward local competition does not guarantee that a given community will actually have a choice of access providers. The criteria proposed by GTE would ensure that customers really have the choice of an alternative provider.

(3) How should price cap regulation evolve as competition develops?
If competition develops in a particular geographical access market, then the FCC's price caps regulation should be streamlined in that market. Access customers then can benefit from the vigorous rivalry among all access providers, including the LEC. GTE's proposal would tie price cap and access regulation streamlining directly to access competition. NYNEX, it would appear, ties the elimination of sharing under an unchanging regime of price cap regulation to the presence of state local competition policies.

As GTE has suggested previously in this proceeding, the elimination of sharing should not be viewed as an end, but a means for the Commission to introduce and rely on competition in access markets. A pure price cap plan would permit the Commission to proceed with selective streamlining in competitive access markets while retaining price cap protection for carriers and consumers in markets where competition had not yet been demonstrated. Under NYNEX's prescription for sharing, the "base-line" portion of their proposal would tighten the sharing bands as compared with the current rules. This would move the

Commission's access regulation closer to rate of return and farther from "pure" price caps. Only in the final step would NYNEX advocate the elimination of sharing.

The elimination of sharing is not an end product of adaptive regulation for access, but a necessary condition to make adaptive regulation possible. A pure price cap plan also would eliminate the need for Commission oversight of LEC depreciation rates and provide an added measure of protection against cross-subsidy of video dialtone services, if the Commission finds it necessary in CC Docket No. 87-266.

Each of these are valid reasons for eliminating sharing. However, none of them have to do with state regulation of local markets. If a pure price caps plan for interstate access is in the public interest — and GTE believes it is — then the Commission should adopt such a change on its merits, rather than use it as a "carrot" to induce desired changes in state regulation, where NYNEX's proposal logically seems to lead.

In summary, GTE agrees with NYNEX that sharing should be eliminated. GTE also agrees that price cap regulation should be adjusted depending on competitive criteria in relevant markets. GTE has already proposed a plan that examines the right market (interstate access, not local), that applies the right criteria (actual competition in a given access market, not state action in local markets), and which takes the correct action (streamlining in competitive access markets) when the criteria are met. This plan will help access markets produce tangible competitive benefits for access customers while ensuring full price cap regulation continues in those markets where competition has yet to develop.

GTE urges the Commission to take the necessary steps in its price caps order, and through a further rulemaking initiative in this proceeding, to develop this approach. Please let me know if you have any questions in the interim.

Sincerely,

Geoffrey C. Gould
Vice President - Government and Federal Regulatory Affairs

c: Office of Commissioner A. Barrett
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